

*M. H.
J.W.H.*

OGC HAS REVIEWED.

16 March 1954

MEMORANDUM FOR: Assistant Comptroller

SUBJECT : Reporting Tax Aspects of Repayment of Excess of
Salary Received in Prior Year

REFERENCES : Memorandum for Assistant Comptroller from Office
of General Counsel, dated 5 January 1954, subject:
Liquidation of Overpayment of Terminal Leave; Staff
Agent .

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1. The reference advised that this office saw no authority under existing federal income tax laws and regulations for a cash basis taxpayer to report on his return net salary in any year in which he has repaid an excess of salary received under claim of right in a prior year. The reference went on to state "Inasmuch as the effect of the procedure, which you indicate is presently followed, may be to afford an unwarranted tax benefit to certain employees under circumstances that are not directly related to the peculiar functions of this Agency, we do not believe that it can be given blanket legal sanction except where recognition is obtained from the Internal Revenue Service of particular circumstances unique to CIA which justify non-application of the strict claim of right test." We indicated that we had discussed the nature of the problem in general terms with cleared officials of IRS and that these officials assured us that they understood the nature of the difficulty and would advise us whether they felt that certain of our situations fell within the claim of right rule.

2. In a meeting on 11 March 1954, IRS representatives informed us of the conclusions which they had reached after consideration of this problem. These conclusions evidence that they fully appreciate the inherent difficulties in maintaining accurate payroll accounts under our complicated cover arrangements.

3. We were told that the IRS agreed, where overpayments were made by the Agency by reason of the unavailability or inaccuracy of information received regarding amounts paid the individual by his cover employer, they were not made or received under "claim of right." In these situations which obviously are peculiar to CIA, IRS indicated that the taxpayer should report as taxable income that amount which properly should have been paid him during the year in question. This would obviate the need in subsequent years when an overpayment was discovered and repaid of adjusting a prior year's return or claiming a deduction in the year in

which repaid. We consider that this relaxation of the strict claim of right rule must be limited to cases which are unique to CIA and should not be allowed in situations which are simply the result of carelessness or administrative oversight.

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Office of General Counsel

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